Lessons

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### Module 1 Review

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## Review Classmates: Module 1 Mini-Project

|  |  |
| --- | --- |
| **Reviews** | 5 complete |

**Well done!**

You've sent 5 classmates valuable feedback that will help them improve. You can review another submission below or you can continue the course.

BMW Interior Mirrors & Fresh Foods Company



by Mohammad Reda

Submitted on July 16, 2016

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## Part 1

For **each of the two decisions** you choose:

Describe a specific setting, the decision, decision alternatives, and any other information that would comprise an interesting and challenging problem.

**1st Make or Buy Decisions (BMW):**

**BMW** for cars manufacturing, currently need to take a decision for its X6 model Car Interior Mirrors, whether to manufacture them inside the factory or to buy them from external supplier. Quantity required is **10,000** unit, the supplier offer to sell them with a unit price **$35**. Knowing that if we will **NOT** manufacture the mirrors inside BMW's factories, we'll save a space for another product line which will provide additional **$45,000**profit for BMW.

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**2nd Keep or Drop Product Line (Fresh Foods):**

**Fresh Foods** for Juice, Chocolate and Ice Cream manufacturing, After reviewing financial statements for 2015 fiscal year, currently need to take a decision whether or not to keep or drop one of its product lines. Two of the product lines provide profits, however the last product line is making losses for the company.

Ice Cream requires a huge fridge for cooling, which is rented for $20,000.

Read the response to Part 1 and assign points below. Be sure to see the detailed rubric on the Instructions tab before assigning points.

* 0 pts - 0 Points: No answer, completely irrelevant answer.
* 5 pts - 5 points: Insufficient, incomplete, lacks supporting evidence.
* 7 pts - 7 points: passing, meets expectations.
* 9 pts - 9 points: Well above average, exceeds expectations.
* 10 pts - 10 points: Superior performance, excellent.

## Part 2

For **each of the two decisions** you choose:

Create a "deliverable" list for the person who would be completing the problem. This deliverable list should be comprised of (at least) two calculations and (at least) one qualitative discussion deliverable (i.e., requiring explanation, additional considerations, etc).

**1st Make or Buy Decisions (BMW) :**

BMW, The costing department has estimated the following costs in case BMW decided to manufacture the 10,000 interior mirrors instead of buying them:

* Direct Material $250,000
* Direct Labor $50,000
* Variable OH $30,000
* Machine Depreciation $20,000
* Fixed OH $50,000
* n Total Manufacturing costs $400,000

**1st** we should determine which cost category is relevant to our decision so we use them in calculations, and which isn't relevant and therefore should be ignored:

* Relevant: Direct Materials + Direct Labor + Variable OH = 250,000 + 50,000 + 30,000
* Irrelevant: Machine Depreciation + Fixed OH = 20,000 + 50,000

**2nd** Now calculating cost per unit

= (Direct Materials + Direct Labor + Variable OH) / 10,000

= (250,000 + 50,000 + 30,000) / 10,000 = 330,000 / 10,000 = $33 per unit

**3rd** The difference between Buying and Manufacturing the interior mirrors:

= (Unit Purchase Price – Unit Manufacturing Costs) \* Number of Units required

= ($35 - $33) \* 10,000

= $2 \* 10,000 = $20,000 savings if BMW decided to manufacture the quantity in house.

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**2nd Keep or Drop Product Line (Fresh Foods):**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Juice | Chocolate | Ice Cream |
| Sales revenue | $650,000 | $450,000 | $80,000 |
| Variable expenses | $325,000 | $370,000 | $70,000 |
| Contribution margin | $325,000 | $80,000 | $10,000 |
| Fixed expenses | $100,000 | $45,000 | $25,000 |
| Net income | $225,000 | $35,000 | ($15,000) |

Read the response to Part 2 and assign points below. Be sure to see the detailed rubric on the Instructions tab before assigning points.

* 0 pts - 0 points: No answer, completely irrelevant answer.
* 5 pts - 5 points: Insufficient, incomplete, lacks supporting evidence.
* 7 pts - 7 points: Passing, meets expectations.
* 9 pts - 9 points: Well above average, exceeds expectations.
* 10 pts - 10 points: Superior performance, excellent

## Part 3

For **each of the two decisions** you choose:

In general, ensure that your exercise tests the person's knowledge related to the use of relevant information in decision making. That is, your exercise should contain some relevant and some "irrelevant" information, so that the person must distinguish between the two types of information. Further, your exercise should allow the person to demonstrate their understanding related to at least two of the following items:

* Opportunity costs
* Sunk costs
* Allocated fixed costs
* Fixed-cost per unit information

**1st Make or Buy Decisions (BMW) :**

Indeed, any report should contain a lot of information, which we should not depend on all of them. We should determine the nature and usage of each cost item, and relate them to the decision process.

Depreciation in this case is irrelevant, so we should exclude the number out of the equation, besides Fixed OH costs as well.

Also, it's not a pure financial decision, we should include hidden costs as opportunity costs and sunk costs as well, which may have significant impact on our decision.

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**2nd Keep or Drop Product Line (Fresh Foods):**

As for this type of decisions, we should look beyond abstract numbers, it's not a matter of negative net income that should attract us, we should have look for what costs this product line is bearing not only for itself, but for the whole factory as well. Allocated Fixed Costs is an example for this, in this type of costs, the product is bearing a share from the factory's whole fixed cost, this portion would be allocated back to other product lines in case we've decided to take this one down.

Read the response to Part 3 and assign points below. Be sure to see the detailed rubric on the Instructions tab before assigning points.

* 0 pts - 0 points: No answer, completely irrelevant answer.
* 5 pts - 5 points: Insufficient, incomplete, lacks supporting evidence.
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## Part 4

Finally, provide a solution for your exercise.

**1st Make or Buy Decisions (BMW) :**

However, that was analysis of financial perspective, if we put in consideration the Opportunity Cost by using the space required for manufacturing the mirrors in house, for another product line to increase profit by $45,000, So, we should compare the figures as we see the big picture now:

Details || Manufacturing || Buying

Cost of product || $330,000 || $350,000

Opportunity Cost || + $45,000 ||

Total Cost || $375,000 || $350,000

It turned out eventually that BUYING interior mirrors from outside supplier has **lower cost** for BMW, than manufacturing the product inside the house.

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**2nd Keep or Drop Product Line (Fresh Foods):**

Looking into the data, we'd start analyzing numbers as follows:

* 1- Calculating status quo for the whole company revenue:

= Juice + Chocolate + Ice Cream

= $650,000 + $450,000 + $80,000 = $1,180,000

* 2- Subtracting lost revenue in case we decided to drop Ice Cream Line = $80,000
* 3- Adding Variable Expenses to the equation = $70,000

Therefore, the total revenue will equal = $1,170,000

However, as mentioned above, Ice Cream requires a huge fridge for cooling, which is rented for $20,000.

* 4- Total Revenue + Saved Fixed Costs = $1,170,000 + $20,000 = $1,190,000

So, It's a **Favorable** decision to **DROP** the Ice Cream Product Line.

Read the response to Part 4 and assign points below. Be sure to see the detailed rubric on the Instructions tab before assigning points.

* 0 pts - 0 points: No answer, completely irrelevant answer.
* 5 pts - 5 points: Insufficient, incomplete, lacks supporting evidence.
* 7 pts - 7 points: Passing, meets expectations.
* 9 pts - 9 points: Well above average, exceeds expectations.
* 10 pts - 10 points: Superior performance, excellent.

Please share constructive comments about the responses. What is one strength of the submissions? What is one area of improvement that you would like to suggest?

Submit Review

### Comments

Visible to classmates